ORIGINAL

OPEN MEETING

0000109539

MEMORANDUM

RECEIVED

2010 MAR 30 P 2: 59

AZ CORP COMMISSION
DOCKET CONTROL

Arizona Corporation Commission
DOCKETED
MAR 30 2010
DOCKETED BY

TO: THE COMMISSION

FROM: Utilities Division

DATE: March 30, 2010

RE: TUCSON ELECTRIC POWER COMPANY. - APPLICATION FOR APPROVAL OF A FUNDING MECHANISM FOR UTILITY-OWNED RENEWABLE ENERGY PROJECTS (DOCKET NO. E-01933A-09-0340)

On July 1, 2009, Tucson Electric Power Company ("TEP" or "Company") filed with the Arizona Corporation Commission ("Commission") a request for approval of its 2010 Renewable Energy Standard and Tariff ("REST") Implementation Plan. As part of its application, TEP sought Commission approval of a number of purchased power contracts and renewable energy projects. In Decision No. 71465 (January 26, 2010), the Commission approved an amended REST Implementation Plan, but did not act on TEP's request for pre-approval of a number of contracts and projects. At the January 12 and 13, 2010 Open Meeting, there was discussion regarding how to finance renewable energy projects which would be owned by TEP. TEP's initial proposal in this proceeding would have recovered the costs of an expansion of its Springerville photovoltaic facility as well as construction of the Tucson Airport tracker project through a one-time pass-through of costs through the REST adjustor mechanism. TEP has previously reported in this proceeding that the Springerville project would cost $7.3 million and the Tucson Airport tracker project would cost $6.7 million. The Commission rejected this approach and asked the Company to present one or more alternative funding options.

The Springerville project includes two expansions of the Company's photovoltaic system at the Springerville Generating Station. Currently TEP has approximately 4.6 MW of photovoltaic generation at the Springerville facility. One part of TEP's proposal includes the installation of four blocks of thin film modules providing 1 MW at a cost of $4 million. Another portion of the project also includes the installation of six blocks of crystalline panels providing 0.81 MW at a cost of $3.3 million. TEP has indicated that these buildouts of the Springerville system could be accomplished relatively quickly, probably by the end of 2010.

The Tucson Airport project is a 1.6 MW single-axis solar tracker that was planned to be part of a wider project called the TEP Storage Project. The 1.6 MW single-axis tracker would be located at the Tucson International Airport and would be designed and constructed by SOLON Corporation. The project would use 350 or 375 watt photovoltaic panels, with 384 modules per array, with 11 or 12 arrays used depending on the wattage of the panels used. The cost of the single-axis tracker would be approximately $6.7 million. TEP initially proposed this project as part of a larger project that would include a storage component if American Recovery and Reinvestment Act ("ARRA") funds were acquired for that portion. TEP did not receive ARRA funds and at this time will not pursue the storage component, but could at a later time. TEP has indicated to Staff that the single-axis tracker project could be constructed under a very short time frame, probably by the end of 2010.

On February 26, 2010, TEP filed a document in this proceeding, requesting Commission approval of a funding mechanism whereby annual costs are recovered through the REST adjustor mechanism until such time as the costs are included in TEP's rate base in its next general rate proceeding. Specifically, TEP requests approval of inclusion of certain costs in the REST adjustor mechanism to cover return on investment, depreciation, property taxes, and operations and maintenance costs beginning in 2011 as part of TEP's 2011 REST plan. TEP estimates those costs would be $1.76 million in 2011, $1.66 million in 2012, and $1.59 million in 2013, and similar costs in following years if no rate case occurs. TEP is not seeking revision of its 2010 REST adjustor rate or caps to recover any of these costs in 2010. The numbers below are based on a 20-year amortization, assuming the first year is 2011. The table below breaks out the cost components of these annual numbers.

Springerville Expansion	2011	2012	2013
Return on Investment	$500,082	$447,413	$386,574
Book Depreciation	$358,716	$358,716	$358,716
Property Tax Expense	$0	$0	$17,341
Operations and Maintenance	$25,000	$25,750	$26,523
Total Springerville Cost	**$883,798**	**$831,880**	**$789,153**
Airport Project			
Return on Investment	$494,936	$442,810	$382,596
Book Depreciation	$355,025	$355,025	$355,025
Property Tax Expense	$0	$0	$34,194
Operations and Maintenance	$25,000	$25,750	$26,523
Total Airport Project	**$874,961**	**$823,585**	**$798,338**
Total TEP			
Return on Investment	$995,018	$890,223	$769,170
Book Depreciation	$713,741	$713,741	$713,741
Property Tax Expense	$0	$0	$51,535
Operations and Maintenance	$50,000	$51,500	$53,045
Total Annual Cost	**$1,758,759**	**$1,655,464**	**$1,587,491**

By comparison, the following tables show the costs if they were amortized over a 3-year or 5-year period for recovery through the REST adjustor mechanism.

3-Year Amortization

Total TEP	2011	2012	2013	2014	2015	2016
Return on Investment	$995,018	$733,181	$408,482	$150,726	$90,477	$30,228
Book Depreciation	$4,758,274	$4,758,274	$4,758,274	$0	$0	$0

Property Tax Expense	$0	$0	$45,481	$44,164	$42,753	$0
Operations and Maintenance	$50,000	$51,500	$53,045	$0	$0	$0
Total Annual Cost	**$5,803,291**	**$5,542,955**	**$5,265,282**	**$194,890**	**$133,230**	**$30,228**

5-Year Amortization

Total TEP	2011	2012	2013	2014	2015	2016
Return on Investment	$995,018	$796,118	$534,355	$339,535	$184,882	$30,228
Book Depreciation	$2,854,964	$2,854,964	$2,854,964	$2,854,964	$2,854,964	$0
Property Tax Expense	$0	$0	$45,481	$44,164	$42,753	$0
Operations and Maintenance	$50,000	$51,500	$53,045	$54,636	$56,275	$0
Total Annual Cost	**$3,899,982**	**$3,702,582**	**$3,487,845**	**$3,293,300**	**$3,138,874**	**$30,228**

TEP claims that this funding mechanism is necessary for TEP to pursue renewable energy projects with Company ownership. TEP claims benefits of Company ownership include: cost-effectiveness, increased viability of developing renewable energy resources in Arizona, increased reliability of TEP's system, reduced reliance on purchased power agreements, and balancing of its renewable portfolio.

In Decision No. 71502 (March 17, 2010), the Commission approved funding provisions for the Arizona Public Service Company ("APS") AZ Sun Program that closely parallel the requested funding mechanism. One difference between the TEP request here and the APS program is that the APS program was a multi-year plan whereas TEP only addresses two current projects.

The other difference is that APS' cost recovery is specifically provided for in the settlement agreement in APS' most recent general rate proceeding in Decision No. 71448 (December 30, 2009). There is no such specific authorization for TEP regarding recovery of costs requested in this proceeding by the Company. Staff believes that the language creating the REST adjustor mechanism for TEP can reasonably be read as either allowing or not allowing these costs to be passed through the Company's REST adjustor mechanism. TEP has indicated to Staff that it is of critical importance in moving forward with Company-owned projects to address how the costs of such projects are recovered. Staff believes that TEP's proposal to pass these costs through the REST adjustor mechanism is reasonable and is consistent with the Commission's treatment of similar costs for the APS AZ Sun Program. As the Commission found in regard to the APS AZ Sun Program, Staff believes that it is unclear whether utility-owned renewable energy will prove to be less expensive than renewable energy produced by nonutility-owned projects. Construction of these TEP projects will provide further opportunity to compare utility-owned and nonutility-owned projects.

Staff has previously recommended that the Commission make findings that these projects meet the REST rules requirements, that they are an appropriate part of TEP's energy portfolio, and that prudency issues would be addressed at a later date. These recommendations will be before the Commission at the March 31 and April 1, 2010 Open Meeting.

Staff Recommendations

Staff recommends that the Commission find that recovery of REST funding through the REST adjustor mechanism for the return on investment, depreciation, property taxes, and O&M expenses related to the Springerville Expansion and Tucson Airport projects, until the Company's next rate case, is appropriate and reasonable.

Staff further recommends that the reasonableness and prudency of those costs be examined during the Company's next rate case and that any costs determined not to be reasonable and prudent be refunded by the Company.

Steven M. Olea
Director
Utilities Division

SMO:RGG:lhm\RM

ORIGINATOR: Robert Gray

BEFORE THE ARIZONA CORPORATION COMMISSION

KRISTIN K. MAYES
Chairman
GARY PIERCE
Commissioner
PAUL NEWMAN
Commissioner
SANDRA D. KENNEDY
Commissioner
BOB STUMP
Commissioner

IN THE MATTER OF THE APPLICATION OF TUCSON ELECTRIC POWER COMPANY FOR APPROVAL OF A FUNDING MECHANISM FOR UTILITY-OWNED RENEWABLE ENERGY PROJECTS	DOCKET NO. E-01933A-09-0340 DECISION NO. __________ ORDER

Open Meeting
April 13, 2010
Phoenix, Arizona

BY THE COMMISSION:

FINDINGS OF FACT

1. Tucson Electric Power Company ("TEP" or "Company") is engaged in providing electric service within portions of Arizona, pursuant to authority granted by the Arizona Corporation Commission ("Commission").

2. On July 1, 2009, TEP filed for Commission approval of its 2010 Renewable Energy Standard and Tariff ("REST") Implementation Plan. As part of its application, TEP sought Commission approval of a number of purchased power contracts and renewable energy projects.

3. In Decision No. 71465 (January 26, 2010), the Commission approved an amended REST Implementation Plan, but did not act on TEP's request for pre-approval of a number of contracts and projects.

4. At the January 12 and 13, 2010 Open Meeting, there was discussion regarding how to finance renewable energy projects which would be owned by TEP. TEP's initial proposal in

this proceeding would have recovered the costs of an expansion of its Springerville photovoltaic facility as well as construction of the Tucson Airport tracker project through a one-time pass-through of costs through the REST adjustor mechanism.

5. TEP has previously reported in this proceeding that the Springerville project would cost $7.3 million and the Tucson Airport tracker project would cost $6.7 million. The Commission rejected this approach and asked the Company to present one or more alternative funding options.

6. The Springerville project includes two expansions of the Company's photovoltaic system at the Springerville Generating Station. Currently, TEP has approximately 4.6 MW of photovoltaic generation at the Springerville facility. One part of TEP's proposal includes the installation of four blocks of thin film modules providing 1 MW at a cost of $4 million. Another portion of the project also includes the installation of six blocks of crystalline panels providing 0.81 MW at a cost of $3.3 million. TEP has indicated that these buildouts of the Springerville system could be accomplished relatively quickly, probably by the end of 2010.

7. The Tucson Airport project is a 1.6 MW single-axis solar tracker that was planned to be part of a wider project called the TEP Storage Project. The 1.6 MW single-axis tracker would be located at the Tucson International Airport and would be designed and constructed by SOLON Corporation. The project would use 350 or 375 watt photovoltaic panels, with 384 modules per array, with 11 or 12 arrays used depending on the wattage of the panels used. The cost of the single-axis tracker would be approximately $6.7 million. TEP initially proposed this project as part of a larger project that would include a storage component if American Recovery and Reinvestment Act ("ARRA") funds were acquired for that portion. TEP did not receive ARRA funds and at this time will not pursue the storage component, but could at a later time. TEP has indicated to Staff that the single-axis tracker project could be constructed under a very short time frame, probably by the end of 2010.

8. On February 26, 2010, TEP filed a document in this proceeding, requesting Commission approval of a funding mechanism whereby annual costs are recovered through the REST adjustor mechanism until such time as the costs are included in TEP's rate base in its next general rate proceeding.

9. Specifically, TEP requests approval of inclusion of certain costs in the REST adjustor mechanism to cover return on investment, depreciation, property taxes, and operations and maintenance costs beginning in 2011 as part of TEP's 2011 REST plan. TEP estimates those costs would be $1.76 million in 2011, $1.66 million in 2012, and $1.59 million in 2013, and similar costs in following years if no rate case occurs. TEP is not seeking revision of its 2010 REST adjustor rate or caps to recover any of these costs in 2010. The numbers below are based on a 20-year amortization, assuming the first year is 2011. The table below breaks out the cost components of these annual numbers.

Springerville Expansion	2011	2012	2013
Return on Investment	$500,082	$447,413	$386,574
Book Depreciation	$358,716	$358,716	$358,716
Property Tax Expense	$0	$0	$17,341
Operations and Maintenance	$25,000	$25,750	$26,523
Total Springerville Cost	**$883,798**	**$831,880**	**$789,153**
Airport Project			
Return on Investment	$494,936	$442,810	$382,596
Book Depreciation	$355,025	$355,025	$355,025
Property Tax Expense	$0	$0	$34,194
Operations and Maintenance	$25,000	$25,750	$26,523
Total Airport Project	**$874,961**	**$823,585**	**$798,338**
Total TEP			
Return on Investment	$995,018	$890,223	$769,170
Book Depreciation	$713,741	$713,741	$713,741
Property Tax Expense	$0	$0	$51,535
Operations and Maintenance	$50,000	$51,500	$53,045
Total Annual Cost	**$1,758,759**	**$1,655,464**	**$1,587,491**

10. By comparison, the following tables show the costs if they were amortized over a 3-year or 5-year period for recovery through the REST adjustor mechanism.

3-Year Amortization

Total TEP	2011	2012	2013	2014	2015	2016
Return on Investment	$995,018	$733,181	$408,482	$150,726	$90,477	$30,228
Book Depreciation	$4,758,274	$4,758,274	$4,758,274	$0	$0	$0
Property Tax Expense	$0	$0	$45,481	$44,164	$42,753	$0
Operations and Maintenance	$50,000	$51,500	$53,045	$0	$0	$0
Total Annual Cost	**$5,803,291**	**$5,542,955**	**$5,265,282**	**$194,890**	**$133,230**	**$30,228**

. . .

5-Year Amortization

Total TEP	2011	2012	2013	2014	2015	2016
Return on Investment	$995,018	$796,118	$534,355	$339,535	$184,882	$30,228
Book Depreciation	$2,854,964	$2,854,964	$2,854,964	$2,854,964	$2,854,964	$0
Property Tax Expense	$0	$0	$45,481	$44,164	$42,753	$0
Operations and Maintenance	$50,000	$51,500	$53,045	$54,636	$56,275	$0
Total Annual Cost	**$3,899,982**	**$3,702,582**	**$3,487,845**	**$3,293,300**	**$3,138,874**	**$30,228**

11. TEP claims that this funding mechanism is necessary for TEP to pursue renewable energy projects with Company ownership. TEP asserts the benefits of Company ownership include: cost-effectiveness, increased viability of developing renewable energy resources in Arizona, increased reliability of TEP's system, reduced reliance on purchased power agreements, and balancing of its renewable portfolio.

12. In Decision No. 71502 (March 17, 2010), the Commission approved funding provisions for the Arizona Public Service Company ("APS") AZ Sun Program that closely parallel the requested funding mechanism.

13. There are several differences between the APS AZ Sun Program and the TEP request. One difference between the TEP request here and the APS program is that the APS program was a multi-year plan whereas TEP only addresses two current projects. The other difference is that APS' cost recovery is specifically provided for in the settlement agreement in APS' most recent general rate proceeding in Decision No. 71448 (December 30, 2009). There is no such specific authorization for TEP regarding recovery of costs requested in this proceeding by the Company.

14. Staff believes that the language creating the REST adjustor mechanism for TEP can reasonably be read as either allowing or not allowing these costs to be passed through the Company's REST adjustor mechanism. TEP has indicated to Staff that it is of critical importance in moving forward with Company-owned projects to address how the costs of such projects are recovered.

15. Staff believes that TEP's proposal to pass these costs through the REST adjustor mechanism is reasonable and is consistent with the Commission's treatment of similar costs for the APS AZ Sun Program. As the Commission found in regard to the APS AZ Sun Program, Staff believes that it is unclear whether utility-owned renewable energy will prove to be less expensive than renewable energy produced by nonutility-owned projects. Construction of these TEP projects will provide further opportunity to compare utility-owned and nonutility-owned projects.

16. Staff has previously recommended that the Commission make findings that these projects meet the REST rules requirements, that they are an appropriate part of TEP's energy portfolio, and that prudency issues would be addressed at a later date. These recommendations will be before the Commission at the March 31 and April 1, 2010 Open Meeting.

17. Staff has recommended that the Commission find that recovery of REST funding through the REST adjustor mechanism for the return on investment, depreciation, property taxes, and O&M expenses related to the Springerville Expansion and Tucson Airport projects, until the Company's next rate case, is appropriate and reasonable.

18. Staff has further recommended that the reasonableness and prudency of those costs be examined during the Company's next rate case and that any costs determined not to be reasonable and prudent be refunded by the Company.

CONCLUSIONS OF LAW

1. TEP is an Arizona public service corporation within the meaning of Article XV, Section 2, of the Arizona Constitution.

2. The Commission has jurisdiction over TEP and over the subject matter of the application.

3. The Commission, having reviewed the application and Staff's Memorandum dated March 30, 2010, concludes that it is in the public interest to approve the funding mechanism, as discussed herein.

ORDER

IT IS THEREFORE ORDERED that recovery of REST funding through the REST adjustor mechanism beginning in 2011, for the return on investment, depreciation, property taxes, and

O&M expenses related to the Springerville Expansion and Tucson Airport projects, until the Company's next rate case, is appropriate and reasonable.

IT IS FURTHER ORDERED that the reasonableness and prudency of those costs be examined during the Company's next rate case and that any costs determined not to be reasonable and prudent be refunded by the Company.

IT IS FURTHER ORDERED that this Decision shall become effective immediately.

BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION

CHAIRMAN COMMISSIONER

COMMISSIONER COMMISSIONER COMMISSIONER

IN WITNESS WHEREOF, I, ERNEST G. JOHNSON, Executive Director of the Arizona Corporation Commission, have hereunto, set my hand and caused the official seal of this Commission to be affixed at the Capitol, in the City of Phoenix, this _______ day of __________________, 2010.

ERNEST G. JOHNSON
EXECUTIVE DIRECTOR

DISSENT: ____________________________

DISSENT: ____________________________

SMO:RGG:lhm\RM

SERVICE LIST FOR: Tucson Electric Power Company
DOCKET NO. E-01933A-09-0340

Mr. Scott Wakefield
201 North Central Avenue, Suite 3300
Phoenix, Arizona 85004-1052

Mr. Daniel Haws
OSJA, ATTN: ATZS-JAD
USA Intelligence Center and Ft. Huachuca
Ft. Huachuca, Arizona 85613-6000

Mr. Peter Nyce
U.S. Legal Services Agency
901 North Stuart Street – 713
Arlington, Virginia 22203-1837

Mr. Dan Neidlinger
Neidlinger & Associates
3020 North 17th Drive
Phoenix, Arizona 85015

Mr. Michael Patten
Roshka, DeWulf & Patten, LLC
One Arizona Center
400 East Van Buren Street – 800
Phoenix Arizona 85004

Mr. C. Webb Crockett
3003 North Central Avenue – 2600
Phoenix, Arizona 85012-2913

Mr. Philip Dion
Tucson Electric Power Company
One South Church Avenue, Suite 200
Tucson, Arizona 85701-1623

Mr. Steven M. Olea
Director, Utilities Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Ms. Janice M. Alward
Chief Counsel, Legal Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007